

- ii. The Debtor has complied with the applicable provisions of the Bankruptcy Code.
- iii. Such Plan has been proposed in good faith and not by any means forbidden by law.
- iv. Any payment made or to be made by the Debtor, or by an entity issuing securities, or acquiring property under such Plan, for services or for costs and expenses in, or in connection with, the Chapter 11 Case or in connection with such Plan and incident to the Chapter 11 Case has been approved by, or is subject to the approval of, the Bankruptcy Court as reasonable.
- v. The Debtor has disclosed the identity and affiliations of any individual proposed to serve, after confirmation of such Plan, as a director or officer of Reorganized XO, and (a) the appointment to or continuance in such office by such individual must be consistent with the interests of Holders of Claims and Creditors' Interests and with public policy and (b) the Debtor has disclosed the identity of any "insider" who will be employed or retained by Reorganized XO and the nature of any compensation for such "insider."
- vi. With respect to each Impaired Class of Claims or Interests, each Holder of a Claim or Interest in such Class has either accepted such Plan or will receive or retain under such Plan on account of such Claim or Interest property of a value, as of the Effective Date, that is not less than the amount that such holder would receive or retain if the Debtor was liquidated on the Effective Date under Chapter 7 of the Bankruptcy Code.
- vii. With respect to each Class of Claims or Interests, such Class has either accepted such Plan or is not Impaired by such Plan. If this requirement is not met, such Plan may still be confirmed pursuant to section 1129(b) of the Bankruptcy Code.
- viii. Except to the extent that the Holder of a particular Claim has agreed to a different treatment of its Claim, such Plan provides that (a) allowed Administrative Expenses will be paid in full in Cash on the Effective Date, (b) Allowed Priority Claims will be paid in full in Cash on the Effective Date, or if the Class of such Claims accepts such Plan, such Plan may provide for deferred Cash payments, of a value as of the Effective Date, equal to the Allowed amount of such Claims, and (c) the Holder of an Allowed Priority Tax Claim will receive on account of such Claim deferred Cash payments over a period not exceeding six years after the date of assessment of such Claim, of a value, as of the Effective Date, equal to the Allowed amount of such Claim.

- ix. If a Class of Claims is Impaired under such Plan, at least one Class of Claims that is Impaired by such Plan has accepted such Plan, determined without including any acceptance of such Plan by any "insider."
- x. Confirmation of such Plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the Debtor or any successor of the Debtor under such Plan.
- xi. All fees payable under section 1930 of title 28 as determined by the Bankruptcy Court at the Confirmation Hearing have been paid or such Plan provides for the payments of all such fees on the Effective Date.
- xii. Such Plan provides for the continuation after the Effective Date of payment of all Retiree Benefits (as defined in section 1114 of the Bankruptcy Code), at the level established pursuant to subsection 1114(e)(1)(B) or 1114(g) of the Bankruptcy Code at any time prior to confirmation of such Plan, for the duration of the period for which the Debtor has obligated themselves to provide such benefits.

The Debtor believes that both Alternatives under the Plan satisfy all of the statutory requirements of Chapter 11 of the Bankruptcy Code. Certain of these requirements are discussed in more detail below.

b. Unfair Discrimination and Fair and Equitable Tests

The Bankruptcy Code contains provisions for confirmation of a plan even if the plan is not accepted by all impaired classes, as long as at least one impaired class of claims has accepted the plan. The "cramdown" provisions of the Bankruptcy Code are set forth in section 1129(b) of the Bankruptcy Code. Under section 1129(b), upon the request of a plan proponent, the bankruptcy court will confirm a plan despite the lack of acceptance by an impaired class or classes if the bankruptcy court finds that (i) the plan does not discriminate unfairly with respect to each non-accepting impaired class, (ii) the plan is fair and equitable with respect to each non-accepting impaired class, and (iii) at least one impaired class has accepted the plan. These standards ensure that holders of junior interests, such as common shareholders, cannot retain any interest in the debtor under a plan of reorganization that has been rejected by a senior class of impaired claims or interests unless such impaired claims or interests are paid in full.

A plan does not discriminate unfairly if claims or interests in different classes but with similar priorities and characteristics receive or retain property of similar value under a plan or, to the extent value is not similar, the disparate treatment is supported by legitimate reasons. By establishing separate Classes for the Holders of each type of Claim or Interest and by treating each Holder of a Claim or Interest in each Class identically and similar Claims or Interests in different Classes similarly, both Alternatives under the Plan have been structured so that similar Claims or Interests in the same Class or different Classes receive similar treatment. As a result,

the Plan does not “discriminate unfairly” within the meaning of section 1129(b) of the Bankruptcy Code as to any impaired Class of Claims or Interests.

The Bankruptcy Code provides a non-exclusive definition of the phrase “fair and equitable.” Section 1129(b)(2) of the Bankruptcy Code establishes tests for determining what is “fair and equitable” for secured creditors, unsecured creditors and equity Holders, as follows:

- i. *Secured Creditors.* Either (1) each impaired secured creditor retains its liens securing its secured claim and receives on account of its secured claim deferred cash payments having a present value equal to the amount of its allowed secured claim, (2) each impaired secured creditor realizes the “indubitable equivalent” of its allowed secured claim, or (3) the property securing the claim is sold free and clear of liens, with such liens to attach to the proceeds of the sale and the treatment of such liens with respect to such proceeds to be as provided in clause (1) or (2) of this subparagraph.
- ii. *Unsecured Creditors.* Either (1) each impaired unsecured creditor receives or retains, under the plan, property of a value equal to the amount of its allowed claim or (2) the holders of claims and interests that are junior to the claims of the dissenting class will not receive any property under the Plan.
- iii. *Equity Interests.* Either (1) each holder of an equity interest will receive or retain, under the plan, property of a value equal to the greatest of the fixed liquidation preference to which such holder is entitled, the fixed redemption price to which such holder is entitled, or the value of the interest or (2) the holder of an interest that is junior to the non-accepting class will not receive or retain any property under the plan.

In general, the provisions of section 1129(b) permit confirmation, notwithstanding non-acceptance by an impaired class, if that class and all junior classes are treated in accordance with the “absolute priority” rule, which requires that a dissenting class be paid in full before a junior class may receive anything under a plan of reorganization on account of their claims or interests. Case law surrounding section 1129(b) requires that no class senior to a non-accepting impaired class receives more than payment in full on its claims.

In the event that either Class 5 (General Unsecured Claims) or Class 6 (Senior Note Claims) does not accept the applicable Alternative under Plan, in order to confirm such Plan, the Debtor must demonstrate to the Court that either (i) each Holder of a Claim in the non-accepting Class will receive or retain under such Plan property of a value equal to the allowed amount of its Claim, or (ii) the Holders of Claims or Holders of Interests that are junior to the Claims of the Holders of such Claims will not receive or retain on account of such Claims or Interests any property under such Plan. Additionally, the Debtor must demonstrate that the Holders of Claims that are senior to the Claims in such non-accepting Class will receive no more than payment in full on their Claims under such Plan. If either Class 5 (General Unsecured

Claims) or Class 6 (Senior Notes Claims) votes to reject either Alternative under the Plan, the Debtor believes that both Alternatives under the Plan nevertheless satisfy these standards. Specifically, whether the FL/Telmex Plan or the Stand-Alone Plan is consummated, the Holders of Claims and Interests that are junior to the Claims in Classes 5 and 6 will receive no property under such Plan on account of their Claims or Interests and no Holder of a Claim that is senior to the Claims in such Classes will receive more than payment in full under such Plan. The fact that, under the Stand-Alone Plan, Claims and Interests in Classes 7 (Subordinated Note Claims), 9 (Old Preferred Stock Interests) and 10 (Old Common Stock Interests) will receive a redistribution of Nontransferable Rights does not violate the "absolute priority" rule because such Rights are being made as a redistribution of property distributed to Class 1 (Senior Secured Lender Claims).

If all the applicable requirements for confirmation of an Alternative under the Plan are met as set forth in sections 1129(a)(1) through (13) of the Bankruptcy Code, except that one or more Classes of impaired Claims have failed to accept such Plan pursuant to section 1129(a)(8) of the Bankruptcy Code, the Debtor intends to request that the Court confirm such Plan in accordance with section 1129(b) of the Bankruptcy Code. The Debtor believes that both Alternatives under the Plan satisfy the "cramdown" requirements of the Bankruptcy Code and may seek confirmation of either Alternative over the objection of dissenting Classes, as well as over the objection of individual Holders of Claims who are members of an accepting Class

In addition, the Debtor intends to seek "cramdown" of either Alternative under the Plan on all Classes of Claims and Interests which are deemed to have rejected the applicable Alternative under the Plan. In such case, the Debtor will request confirmation of such Plan under section 1129(b) of the Bankruptcy Code notwithstanding the deemed rejection of such Plan by Classes 7, 8, 9, 10 and 11. The Debtor believes that both Alternatives under the Plan may be confirmed pursuant to the above-described "cramdown" provision, over the deemed dissent of Holders of Claims or Interests in such Classes in view of the treatment proposed for such Classes. Specifically, XO believes that the treatment under both Alternatives under the Plan of the Holders of Interests or Claims in Classes 7, 8, 9, 10 and 11 satisfies the "fair and equitable" test since there is no Class junior to such non-accepting Classes that is entitled to receive or retain any property under either Alternative under the Plan.

c. Best Interests Test

With respect to each Impaired Class of Claims and Interests, confirmation of either Alternative under the Plan requires that each Holder of a Claim or Interest either (a) accept such Plan or (b) receive or retain under such Plan property of a value, as of the Effective Date, that is not less than the value such Holder would receive or retain if the Debtor was liquidated under Chapter 7 of the Bankruptcy Code. To calculate the probable distribution to Holders of each Impaired Class of Claims and Interests if the Debtor was liquidated under Chapter 7, a bankruptcy court must first determine the aggregate dollar amount that would be generated from the Debtor's assets if its Chapter 11 Case were converted to a Chapter 7 case under the Bankruptcy Code. This "liquidation value" would consist primarily of the proceeds from a forced sale of the Debtor's assets by a Chapter 7 trustee.

To estimate potential returns to Holders of Claims and Interests in a Chapter 7 liquidation, the Debtor determined, as might a Bankruptcy Court conducting such an analysis, the amount of cash liquidation proceeds that might be available for distribution and the allocation of such proceeds among the Classes of Claims and Interests of XO based on their relative priorities. The Debtor considered many factors and data, including (i) the operating and financial performance of XO, (ii) the attractiveness of the assets of XO, respectively, to potential buyers, (iii) the potential universe of buyers, (iv) the potential impact of the Chapter 7 cases upon the businesses of the Debtor, as well as on the realizable value from the liquidation of the non-cash assets of XO, (v) the relative timing of the potential sale of the Debtor's assets, and (vi) an analysis of the liabilities and obligations of XO. For the purposes of this analysis, the Debtor has assumed that the liquidation of all assets would be conducted in an orderly, yet expedited, manner over a six-month period commencing on September 30, 2002. The liquidation proceeds available to XO for distribution to Holders of Claims against and Interests in XO, respectively, would consist of the net proceeds from the disposition of the assets of XO, augmented by any other cash held after deducting the expenses of operating the business pending disposition and the costs associated with the disposition of the non-cash assets of the XO.

In general, liquidation proceeds would be allocated in the following priority: (i) first, to the Claims of secured creditors to the extent of the value of their collateral; (ii) second, to the costs, fees and expenses of the liquidation, as well as other administrative expenses of the Debtor's Chapter 7 cases, including tax liabilities; (iii) third, to the unpaid Administrative Claims of reorganization cases (if commenced); (iv) fourth, to Priority Tax Claims and other Claims entitled to priority in payment under the Bankruptcy Code; (v) fifth, to unsecured Claims; (vi) sixth, to Holders of Old Preferred Stock (in accordance with their relative ranking); and (vii) seventh, to Holders of Old Common Stock. The Debtor's liquidation costs in their respective Chapter 7 cases would include the compensation of a bankruptcy trustee, as well as compensation of counsel and other professionals retained by such trustee, asset disposition expenses, applicable taxes, litigation costs, Claims arising from the operation of the Debtor during the pendency of the Chapter 7 cases and all unpaid Administrative Claims incurred by the Debtor during the reorganization cases (if commenced) that are allowed in the Chapter 7 case. The liquidation itself might trigger certain Priority Claims, such as Claims for severance pay, and would likely accelerate or, in the case of taxes, make it likely that the Internal Revenue Service would assert other claims as Priority Tax Claims rather than asserting them in due course as is expected to occur under the reorganization cases. These Priority Claims would be paid in full out of the net liquidation proceeds, after payment of secured Claims, Chapter 7 costs of administration and other Administrative Claims, and before the balance would be made available to pay unsecured claims or to make any distribution in respect of Interests.

The Debtor believes that both Alternatives under the Plan meet the "best interests of creditors" test of Section 1129(a)(7) of the Bankruptcy Code. The Debtor believes that the members of each Impaired Class will receive greater or equal value if either the FL/Telmex Plan or the Stand-Alone Plan was consummated than they would in a liquidation. The Liquidation Analysis, a copy of which is attached hereto as Appendix C, provides that in the event of a liquidation as described therein, the proceeds available for Holders of Senior Secured Lender Claims in XO would be approximately \$257 million to \$561 million, resulting in a recovery of only 22.6% to 52.2%. The Liquidation Analysis provides that there would be no recovery to Holders of General Unsecured Claims, Senior Note Claims, Subordinated Note Claims,

Securities Claims, Old Preferred Stock Interests, Old Common Stock Interests or Other Old Equity Interests.

In contrast, under the Plan, Senior Secured Lender Claims will receive a 98.1% recovery under the FL/Telmex Plan and 92.6% under the Stand-Alone Plan. Therefore, Holders of such Claims will receive more under either Alternative under the Plan than in a liquidation. Although the Debtor believes that both Alternatives under the Plan meet the "best interests of creditors" test of Section 1129(a)(7) of the Bankruptcy Code, there can be no assurance that the Bankruptcy Court will determine that the applicable Alternative under the Plan meets this test. THESE ESTIMATES OF VALUE ARE SUBJECT TO A NUMBER OF ASSUMPTIONS AND SIGNIFICANT QUALIFYING CONDITIONS. ACTUAL VALUES AND RECOVERIES COULD VARY MATERIALLY FROM THE ESTIMATES SET FORTH HEREIN.

d. Feasibility

The Bankruptcy Code requires that the bankruptcy court determine that confirmation of a plan is not likely to be followed by liquidation or the need for further financial reorganization of the Debtor. For purposes of showing that both Alternatives under the Plan meet this feasibility standard, the Debtor and Houlihan Lokey have analyzed the ability of Reorganized XO to meet its obligations under each of the Alternatives under the Plan and retain sufficient liquidity and capital resources to conduct their business.

The Debtor believes that with a significantly deleveraged capital structure, their business will be able to return to viability. The decrease in the amount of debt on the Company's balance sheet will improve the Company's cash flow by reducing its interest expense. To further support its belief in the feasibility of both Alternatives under the Plan, the Debtor has relied upon Pro Forma Financial Projections for Fiscal Years 2002 through 2005 contained in Appendix B-1 (FL/Telmex Plan) and Appendix B-2 (Stand-Alone Plan) annexed hereto. The Projections indicate that Reorganized XO should have sufficient cash flow to pay and service their debt obligations under the FL/Telmex Plan or under the Stand-Alone Plan. Accordingly, the Debtor believes that both Alternatives under the Plan comply with the financial feasibility standard of Section 1129(a)(11) of the Bankruptcy Code.

Holders of Claims against and Interests in the Debtor are advised, however, that the Projections were not prepared with a view toward compliance with the published guidelines of the American Institute of Certified Public Accountants or any other regulatory or professional agency or body or generally accepted accounting principles. Furthermore, the Debtor's independent certified public accountants have not compiled or examined the Projections and accordingly do not express any opinion or any other form of assurance with respect thereto and assume no responsibility for the Projections.

The Projections also assume that (i) the Plan will be confirmed and consummated in accordance with its terms or the terms of the Investment Agreement or the Stand-Alone Term Sheet, (ii) there will be no material change in legislation or regulations, or the administration thereof, including telecommunications and environmental legislation or regulations, that will have an unexpected effect on the operations of Reorganized XO, (iii) there will be no change in United States generally accepted accounting principles that will have a material effect on the

reported financial results of Reorganized XO and (iv) there will be no material contingent or unliquidated litigation or indemnity claims applicable to Reorganized XO. The assumptions inherent in the Projections are based upon future business decisions and objectives, which differ in Appendix B-1 versus Appendix B-2 based upon the significant difference in the amount of capital available to XO pursuant to the Investment Agreement and the Stand-Alone Term Sheet, and are subject to change. In addition, although they are presented with numerical specificity and considered reasonable by the Debtor when taken as a whole, the assumptions and estimates underlying the Projections are subject to significant business, economic and competitive uncertainties and contingencies, many of which will be beyond the control of Reorganized XO.

Accordingly, the Projections are only estimates that are necessarily speculative in nature. It can be expected that some or all of the assumptions in the Projections will not be realized and that actual results will vary from the Projections, which variations may be material and are likely to increase over time. The Projections should therefore not be regarded as a representation by the Debtor or any other person that the results set forth in the Projections will be achieved. In light of the foregoing, readers are cautioned not to place undue reliance on the Projections. The Projections should be read together with the information in this Disclosure Statement entitled "Risk Factors," which sets forth important factors that could cause actual results to differ from those in the Projections.

XO is subject to the informational requirements of the Exchange Act and in accordance therewith files periodic reports and other information with the SEC (as defined below) relating to its business, financial statements and other matters. Such filings will not include projected financial information. The Debtor does not intend to update or otherwise revise the Projections, including any revisions to reflect events or circumstances existing or arising after the date of this Disclosure Statement or to reflect the occurrence of unanticipated events, even if any or all of the underlying assumptions do not come to fruition. Furthermore, the Debtor does not intend to update or revise the Projections to reflect changes in general economic or industry conditions.

e. Valuation Analysis

In order to comply with the "best interests" test as well as to determine the relative distributions to parties in interest under a potential plan, an estimated transaction value (the "Transaction Value") and recovery analysis (the "Recovery Analysis") has been prepared by Houlihan Lokey, financial advisors to the Company, for both the FL/Telmex Plan and the Stand-Alone Plan. Houlihan Lokey has determined the Transaction Value and Recovery Analysis based on an assumed Effective Date of September 30, 2002 giving effect to the implementation of the Plan.

i. FL/Telmex Plan

In reaching its conclusions regarding the implied Transaction Value and the associated Recovery Analysis relating to the FL/Telmex Plan, Houlihan Lokey analyzed, among other things, (i) the amount of the aggregate purchase price implied by the Investment Agreement and (ii) the form and amount of distributions to Senior Secured Lender Claims, Other Secured Claims and Note Claims pursuant to the Investment Agreement.

Pursuant to the Investment Agreement, Forstmann Little and Telmex have agreed to invest a combined \$800 million in cash in exchange for an 80% ownership interest in Reorganized XO (pre-dilution for common stock to be issued pursuant to the Management Shares Purchase Agreement). The Investment Agreement contemplates (i) the assumption of XO's existing \$1.0 billion in principal amount of Senior Secured Lender Claims, (ii) the assumption of approximately \$24.7 million (estimated as of September 30, 2002) of outstanding capital lease obligations and (iii) the elimination of all Note Claims and Old Preferred Stock Interests pursuant to the restructuring outlined in the Investment Agreement.

Based upon the face amount of the aforementioned securities, the implied aggregate Transaction Value of the FL/Telmex Plan is \$2,025 million, thus implying a pre-money Transaction Value of \$1,425 million.

<i>Transaction Value - FL/Telmex Plan</i>	
<i>(\$ in millions)</i>	
Cash Purchase Price	\$800.0
Post-Transaction Equity Ownership	80.0%
Implied Total Company Equity Value	\$1,000.0
Plus: Restructured Bank Debt	1,000.0
Plus: Capital Lease Obligations	24.7
Aggregate Implied Purchase Price	\$2,024.7
Less: Net Cash Invested in XO <i>(net of \$200 million allocation to Senior Note Claims)</i>	(600.0)
Aggregate Implied Pre-Money Purchase Price	\$1,424.7
<i>Implied Multiple of FY 2001 Revenues</i>	<i>1.1x</i>

The Company reported approximately \$1,259 million of aggregate revenues for the fiscal year ended December 31, 2001. The implied pre-money Transaction Value represents a 1.1x multiple of the Company's fiscal year 2001 revenues, which is comparable to prevailing forward public market valuations of selected other domestic providers of broadband communications services.

The following chart provides a summary overview of the implied recoveries to the Senior Secured Lenders and Note Claims in the context of the FL/Telmex Plan.

Recovery Analysis

<i>(\$ in millions except per share value)</i>	
Implied Forstmann Little and Telmex Transaction Value	\$2,025
Less: Restructured Senior Secured Lender Claims	(1,000)
Less: Capital Lease Obligations <i>(estimated as of 6/30/02)</i>	(25)
Implied Total Restructured Equity Value	\$1,000
Value Allocation & Recoveries:	
Senior Secured Lender Claims:	
Allowed Claim Amount Including Estimated Accrued Interest through September 30, 2002	\$1,028
Amount of Restructured Senior Secured Lender Claims	1,000
Plus: Estimated Accrued Interest as of the Effective Date <i>(to be paid in cash)</i>	28
Less: Senior Secured Lender Waiver of Interest Pursuant to the Shareholder Litigation Settlement	(20)
Total Net Value Allocated to Senior Secured Lender Claims	1,008
Implied Recovery	98.1%
Note Claims: ⁽²⁾	
Allowed Claim Amount ⁽¹⁾ <i>(as of June 16, 2002)</i>	\$3,871
% of Post-Reorganization Equity	17.9%
Implied Equity Value	\$179
Plus: Cash	199
Total Value Allocated to XO Note Claims	\$378
Implied Recovery	9.8%
General Unsecured Claims: ⁽²⁾	
Estimated Claim Amount	\$20
% of Post-Reorganization Equity	0.1%
Implied Equity Value	\$1
Plus: Cash	1
Total Value Allocated to XO Note Claims	\$2
Implied Recovery	8.6%
<i>(1) Represents the aggregate principal balance of the Company's Senior Notes plus accrued and unpaid interest through June 16, 2002, excluding those Senior Notes held by the Company. The Company's Senior Discount Notes reflect estimated accreted values through June 16, 2002.</i>	
<i>(2) Please note that the recoveries to Note Claims and General Unsecured Claims are allocated pro rata after taking into account the subordination provision between the Note Claims and the Subordinated Note Claims.</i>	

ii. Stand-Alone Plan

In reaching its conclusions regarding the implied Transaction Value and the associated Recovery Analysis relating to the Stand-Alone Plan, Houlihan Lokey analyzed, among other things, (i) the amount of the aggregate pre-Rights Offering equity value outlined in the Stand-Alone Term Sheet and (ii) the form and amount of distributions to Senior Secured Lender Claims, Other Secured Claims and Note Claims pursuant to the Stand-Alone Plan.

The Stand-Alone Plan contemplates (i) the elimination of all Senior Secured Lender Claims, Note Claims, Old Preferred Stock Interests and Other Old Equity Interests, (ii) Holders of the Senior Secured Claims receiving (x) \$500 million in aggregate principal amount of New Junior Secured Loans, (y) certain residual rights under the Rights Offering, and (z)(a) if two-thirds or more of the Unaffiliated Senior Note Claims voting with respect to the Stand-Alone Plan vote to approve it, and the Official Committee of Unsecured Creditors has recommended a vote in favor of confirmation of the Stand-Alone Plan and not withdrawn such recommendation,

90,250,000 shares of the New Reorganization Common Stock representing 95% of all issued and outstanding shares of New Reorganization Common Stock (subject to dilution resulting from the exercise of the New Warrants, the issuance of shares pursuant to the Rights Offering and the exercise of New Options under the Management Incentive Program), or (b) if less than two-thirds of the Unaffiliated Senior Note Claims voting with respect to the Stand-Alone Plan vote to approve its confirmation, 95,000,000 shares of the New Reorganization Common Stock representing 100% of all issued and outstanding shares of New Reorganization Common Stock (subject to dilution resulting from the exercise of the New Warrants, the issuance of shares pursuant to the Rights Offering and the exercise of New Options under the Management Incentive Program), (iii) Holders of Senior Note Claims and General Unsecured Claims receiving (x) Nontransferable Rights to purchase up to \$200 million (subject to increase in certain events) of common equity in Reorganized XO; and (y)(a) if two-thirds or more of the Unaffiliated Senior Note Claims voting with respect to the Stand-Alone Plan vote to approve it, and the Official Committee of Unsecured Creditors has recommended a vote in favor of confirmation of the Stand-Alone Plan and not withdrawn such recommendation, 4,750,000 shares of the New Reorganization Common Stock (representing 5% of all issued and outstanding shares of New Reorganization Common Stock on the Effective Date), New Series A Warrants to purchase 9,500,000 shares of New Reorganization Common Stock (representing 10% of all issued and outstanding shares of New Reorganization Common Stock on the Effective Date), New Series B Warrants to purchase 7,125,000 shares of New Reorganization Common Stock (representing 7.5% of all issued and outstanding shares of New Reorganization Common Stock on the Effective Date), New Series C Warrants to purchase 7,125,000 shares of New Reorganization Common Stock (representing 7.5% of all issued and outstanding shares of New Reorganization Common Stock on the Effective Date) and 10% of the FL/Telmex Recovery; or (b) if less than two-thirds of the Unaffiliated Senior Note Claims voting with respect to the Stand-Alone Plan vote to approve its confirmation, but the Official Committee of Unsecured Creditors has recommended a vote in favor of the Stand-Alone Plan, has not withdrawn such recommendation and the Debtor believes, in its reasonable judgment, that all of the members of such Committee have voted their Claims in favor of confirmation of the Stand-Alone Plan, New Series B Warrants to purchase 4,750,000 shares of New Reorganization Common Stock (representing 5% of all issued and outstanding shares of New Reorganization Common Stock on the Effective Date). Additionally, the Stand-Alone Plan provides for a \$200 million new senior secured Exit Facility that will be reduced by up to \$200 million of cash proceeds realized from the Rights Offering.

Based upon the face amount of the New Junior Secured Loans and the pre-Rights transaction equity value outlined in the Stand-Alone Plan, the implied aggregate Transaction Value contemplated by the Stand-Alone Plan is roughly \$1,000 million, thus implying a post-Rights Offering enterprise value of approximately \$1,200 million assuming 100% participation in the Rights Offering by the Hlders of Senior Note Claims and zero participation by the Holders of General Unsecured Claims.¹⁶

¹⁶ The foregoing valuation and recovery analyses were prepared by Houlihan Lokey and do not reflect the opinion of the Holders of Senior Secured Claims or their advisors. In fact, representatives of the Holders of Senior Secured Claims have advised XO that they expressly disagree with these analyses and that they should not be attributed to the Holders of the Senior Secured Claims.

<i>Transaction Value - Stand-Alone Plan</i>	
<i>(\$ in millions)</i>	
Stated Pre-Rights Equity Value	\$475.0
Plus: Estimated Revolver Drawdown (1)	-
Plus: New Junior Secured Loans	500.0
Plus: Capital Lease Obligations	<u>24.7</u>
Aggregate Implied Pre-Rights Enterprise Value (1)	\$999.7
Plus: Rights Offering Proceeds Assuming 100% Subscription	200.0
Aggregate Implied Post-Rights Enterprise Value	\$1,199.7
<i>(1) This analysis excludes maximum net revolver borrowings of approximately \$114 million in Q3-05 in the event that no money is raised in the Rights Offering.</i>	

The following charts provide a summary overview of the implied recoveries to the Senior Secured Lenders and Note Claims in the context of the Stand-Alone Plan assuming (1) two-thirds or more of the Unaffiliated Senior Note Claims voting with respect to the Stand-Alone Plan vote to approve it, the Official Committee of Unsecured Creditors has recommended a vote in favor of confirmation of the Stand-Alone Plan and not withdrawn such recommendation and there is no participation in the Rights Offering, (2) two-thirds or more of the Unaffiliated Senior Note Claims voting with respect to the Stand-Alone Plan vote to approve it, the Official Committee of Unsecured Creditors has recommended a vote in favor of confirmation of the Stand-Alone Plan and not withdrawn such recommendation and there is 100% participation in the Rights Offering by Holders of the Senior Note Claims and zero participation by the Holders of General Unsecured Claims and (3) less than two-thirds of the Unaffiliated Senior Note Claims voting with respect to the Stand-Alone Plan vote to approve its confirmation, but the Official Committee of Unsecured Creditors has recommended a vote in favor of the Stand-Alone Plan, has not withdrawn such recommendation and the Debtor believes, in its reasonable judgment, that all of the members of such Committee have voted their Claims in favor of confirmation of the Stand-Alone Plan and there is no participation in the Rights Offering.

Recovery Analysis - Stand-Alone Plan Assuming No Participation in the Rights Offering (Assuming Official Committee Vote is Obtained)	
Assumed Pre-Rights Enterprise Value	\$1,000
Less: New Revolver Borrowings (future estimated revolver borrowings are excluded for the purposes of this analysis)	-
Less: Capital Lease Obligations	(25)
Less: New Junior Secured Loans	(500)
Implied Pre-Rights Equity Value	\$475
Less: Estimated Value Warrants (1)	38
Less: Estimated Value of Management Options (2)	-
Residual Pre-Rights Offering Equity Value Available for Distribution	\$437
Value Allocation & Recoveries:	
Amount of Outstanding Bank Debt (including accrued interest through June 16, 2002)	\$1,009
% Allocation of Equity Value - Pre Dilution for Warrants, Rights & Mgmt. Options	95.0%
Implied Equity Value	\$415
New Junior Secured Loans (estimated market value)	476
Total Implied Allocated Value	\$891
Implied Recovery	88.4%
Amount of Outstanding Senior Notes and Senior Discount Notes (3) (4)	\$3,872
% Allocation of Equity Value - Pre Dilution for Warrants, Rights & Mgmt. Options	5.0%
Implied Equity Value	\$22
Estimated Value of Warrants (5)	38
Total Implied Allocated Value	\$60
Implied Recovery	1.5%
Amount of General Unsecured Claims (4)	\$20
% Allocation of Equity Value - Pre Dilution for Warrants, Rights & Mgmt. Options	0.0%
Implied Equity Value	\$0
Estimated Value of Warrants (5)	0
Total Implied Allocated Value	\$0
Implied Recovery	1.4%
<p>(1) For the purposes of this analysis, we estimated the value of warrants allocated to the Senior Noteholders on a pre-rights offering basis with respect to shares and implied equity value.</p> <p>(2) For the purposes of this analysis, we have not deducted the value of management options for 7% of the common stock of reorganized XO.</p> <p>(3) Represents the aggregate principal balance of the Company's Senior Notes plus accrued and unpaid interest through June 16, 2002, excluding those Senior Notes held by the Company. The Company's Senior Discount Notes reflect estimated accreted values through June 16, 2002.</p> <p>(4) Please note that the recoveries to Note Claims and General Unsecured Claims are allocated pro rata after taking into account the subordination provision between the Note Claims and the Subordinated Note Claims.</p> <p>(5) The Senior Noteholders and General Unsecured Claims are assumed to be allocated (1) 7-year warrants to purchase 10% of New Common Stock at a 25% premium to the implied pre-rights offering equity value of \$475 million, (2) 7-year warrants to purchase 7.5% of New Common Stock at a 50% premium to the implied pre-rights offering equity value of \$475 million, and (3) 7-year warrants to purchase 7.5% of New Common Stock at a 100% premium to the implied pre-rights offering equity value of \$475 million. For the purposes of this analysis, all warrants are valued assuming a 40% volatility and a 6.0% risk-free rate.</p>	

Recovery Analysis - Stand-Alone Plan Assuming \$200 Million Participation in the Rights Offering
(Assuming Official Committee Vote is Obtained)

Revised Recovery Calculation Post Rights Offering:		
Assumed Pre-Rights Enterprise Value		\$1,000
Implied Pre-Rights Offering Equity Value		\$475
Less: Estimated Value of Warrants (1)		(69)
Less: Estimated Value of Management Options (2)		-
Plus: Proceeds from Rights Offering		200
Residual Post-Rights Offering Equity Value Available for Distribution		\$606
Allocation of Shares in the Rights Offering: (3)		
<i>Assumed Amount & Subscription</i>	<i>Amount</i>	
Senior Notes & Senior Discount Notes	\$200	40.0
General Unsecured Claims	\$0	-
Subordinated Notes	\$0	-
Preferred Stock	\$0	-
Common Stock	\$0	-
Senior Secured Lenders		90.3
Senior Notes & Senior Discount Notes (pre-rights offering)		4.7
General Unsecured Claims		0.0
Total Shares post Rights Offering		135.0
% of Shares Allocated in Rights Offering		29.6%
Amount of Outstanding Bank Debt (including accrued interest through June 16, 2002)		\$1,009
% Allocation of Equity Value - Pre-Dilution for Warrants & Mgmt. Options		66.9%
Implied Equity Value		\$405
New Junior Secured Loans (estimated market value)		476
Total Implied Allocated Value		\$882
Implied Recovery		87.4%
Amount of Outstanding Senior Notes and Senior Discount Notes (4)		\$3,872
% Allocation of Equity Value - Pre Dilution for Warrants & Mgmt. Options		33.1%
Implied Equity Value		\$201
Estimated Value of Warrants (5)		68
Less: Rights Offering Investment		(200)
Total Implied Allocated Value		\$69
Implied Recovery		1.8%
Amount of General Unsecured Claims (6)		\$20
% Allocation of Equity Value - Pre Dilution for Warrants, Rights & Mgmt. Options		0.0%
Implied Equity Value		\$0
Estimated Value of Warrants (5)		0
Less: Rights Offering Investment		-
Total Implied Allocated Value		\$0
Implied Recovery		2.0%
Equity Ownership Percentages Post-Rights Offering:		
Banks		66.9%
Senior Notes & Senior Discount Notes		33.1%
General Unsecured Claims		0.0%
Subordinated Notes		0.0%
Preferred Stock		0.0%
Common Shares		0.0%

- (1) For the purposes of this analysis, we estimated the value of Warrants allocated to the Senior Noteholders on a post-Rights Offering basis with respect to the implied equity value.
- (2) For the purposes of this analysis, we have not deducted the value of management options for 7% of the common stock of reorganized XO.
- (3) Based on pre-Rights Offering equity value assuming 95 million shares are issued. Please note that, for the purposes of this analysis, we do not assume that holders of General Unsecured Claims exercise their Rights.
- (4) Represents the aggregate principal balance of the Company's Senior Notes plus accrued and unpaid interest through June 16, 2002, excluding those Senior Notes held by the Company. The Company's Senior Discount Notes reflect estimated accreted values through June 16, 2002.
- (5) The Senior Noteholders and General Unsecured Claims are assumed to be allocated (1) 7-year warrants to purchase 10% of New Common Stock at a 25% premium to the implied pre-rights offering equity value of \$475 million, (2) 7-year warrants to purchase 7.3% of New Common Stock at a 50% premium to the implied pre-rights offering equity value of \$475 million, and (3) 7-year warrants to purchase 7.5% of New Common Stock at a 100% premium to the implied pre-rights offering equity value of \$475 million. For the purposes of this analysis, all warrants are valued assuming a 40% volatility and a 6.0% risk-free rate.
- (6) Please note that the recoveries to Note Claims and General Unsecured Claims are allocated pro rata after taking into account the subordination provision between the Note Claims and the Subordinated Note Claims.

Recovery Analysis - Stand-Alone Plan Assuming No Participation in the Rights Offering
(Assuming Official Committee Vote is not Obtained, but Official Committee of Unsecured Creditors Votes to Accept the Plan)

Assumed Pre-Rights Enterprise Value	\$1,000
Less: New Revolver Borrowings <i>(future estimated revolver borrowings are excluded for the purposes of this analysis)</i>	-
Less: Capital Lease Obligations	(25)
Less: New Junior Secured Loans	(500)
Implied Pre-Rights Equity Value	\$475
Less: Estimated Value of Warrants ⁽¹⁾	9
Less: Estimated Value of Management Options ⁽²⁾	-
Residual Pre-Rights Offering Equity Value Available for Distribution	\$466
Value Allocation & Recoveries:	
Amount of Outstanding Bank Debt <i>(including accrued interest through June 16, 2002)</i>	\$1,009
% Allocation of Equity Value - Pre Dilution for Warrants, Rights & Mgmt. Options	100.0%
Implied Equity Value	\$466
New Junior Secured Loans <i>(estimated market value)</i>	476
Total Implied Allocated Value	\$942
Implied Recovery	93.4%
Amount of Outstanding Senior Notes and Senior Discount Notes ⁽³⁾ ⁽⁴⁾	\$3,872
% Allocation of Equity Value - Pre Dilution for Warrants, Rights & Mgmt. Options	0.0%
Implied Equity Value	\$0
Estimated Value of Warrants ⁽⁵⁾	9
Total Implied Allocated Value	\$9
Implied Recovery	0.2%
Amount of General Unsecured Claims ⁽⁴⁾	\$20
% Allocation of Equity Value - Pre Dilution for Warrants, Rights & Mgmt. Options	0.0%
Implied Equity Value	\$0
Estimated Value of Warrants ⁽⁵⁾	0
Total Implied Allocated Value	\$0
Implied Recovery	0.2%

(1) For the purposes of this analysis, we estimated the value of warrants allocated to the Senior Noteholders on a pre-rights offering basis with respect to shares and implied equity value.

(2) For the purposes of this analysis, we have not deducted the value of management options for 7% of the common stock of reorganized XO.

(3) Represents the aggregate principal balance of the Company's Senior Notes plus accrued and unpaid interest through June 16, 2002, excluding those Senior Notes held by the Company. The Company's Senior Discount Notes reflect estimated accreted values through June 16, 2002.

(4) Please note that the recoveries to Note Claims and General Unsecured Claims are allocated pro rata after taking into account the subordination provision between the Note Claims and the Subordinated Note Claims.

(5) The Senior Noteholders and General Unsecured Claims are assumed to be allocated 7-year warrants to purchase 5% of New Common Stock at a 50.0% premium to the implied pre-rights offering equity value of \$475 million. For the purposes of this analysis, the warrants are valued assuming a 40% volatility and a 6.0% risk-free rate.

E. Securities Considerations

Upon the consummation of either Alternative under the Plan, XO will rely on Section 1145 of the Bankruptcy Code, to the extent it is applicable, to exempt the issuance of the New Common Stock, Post-Termination Securities and the Conversion Common Stock from the registration requirements of the Securities Act (and of any state securities or "blue sky" laws). Section 1145 exempts from registration the sale of a debtor's securities under a Chapter 11 plan if such securities are offered or sold in exchange for a claim against, or equity interest in, or a claim for an administrative expense in a case concerning, the debtor. In reliance upon this exemption, issuance of the New Common Stock, Post-Termination Securities and Conversion Common Stock, and the issuance of securities upon exercise or conversion thereof, generally will be exempt from the registration requirements of the Securities Act of 1933 (the "Securities Act"). Accordingly, recipients will be able to resell the New Common Stock, Post-Termination Securities or Conversion Common Stock without registration under the Securities Act or other federal securities laws, unless the recipient is an "underwriter" with respect to such securities, within the meaning of Section 1145(b) of the Bankruptcy Code. Section 1145(b) of the Bankruptcy Code defines "underwriter" as one who (a) purchases a claim with a view to distribution of any security to be received in exchange for the claim, or (b) offers to sell securities issued under a plan for the holders of such securities, (c) offers to buy securities issued under a plan from persons receiving such securities, if the offer to buy is made with a view to distribution or (d) is an "issuer" of the relevant security, as such term is used in Section 2(11) of the Securities Act.

Notwithstanding the foregoing, statutory underwriters may be able to sell securities without registration pursuant to the resale limitations of Rule 144 under the Securities Act which, in effect, permits the resale of securities received by statutory underwriters pursuant to a Chapter 11 plan, subject to applicable volume limitations, notice and manner of sale requirements, and certain other conditions. Holders who believe they may be statutory underwriters as defined in Section 1145 of the Bankruptcy Code are advised to consult with their own counsel as to the availability of the exemption provided by Rule 144.

F. Alternatives to Confirmation and Consummation of the Plan

The Debtor believes that both Alternatives under the Plan afford Holders of Claims and Interests the potential for the greatest recovery and, therefore, is in the best interests of such Holders. If, however, the requisite acceptances of either Alternative under the Plan are not received, or the applicable Alternative is not confirmed and consummated, the theoretical alternatives include (a) formulation of an alternative plan of reorganization or (b) liquidation of the Debtor under Chapter 7 or 11 of the Bankruptcy Code.

1. Alternative Plan(s) of Reorganization

Even if the applicable Alternative is uncontested, it is estimated that such Plan will take several months to confirm and could take longer. Furthermore, even if all Classes of Impaired Claims entitled to vote on such Plan voted to accept such Plan, such Plan nevertheless may not be confirmed by the Bankruptcy Court. The Bankruptcy Court, which sits as a court of equity, may exercise substantial discretion. Section 1129 of the Bankruptcy Code sets forth the

requirements for confirmation and requires, among other things, that the confirmation of such Plan not be followed by a need for further financial reorganization and that the value of distributions to dissenting creditors and shareholders not be less than the value of distributions such creditors and shareholders would receive if the Debtor was liquidated under Chapter 7 of the Bankruptcy Code. Although the Debtor believes that both Alternatives under the Plan will meet such tests, there can be no assurance that the Bankruptcy Court would reach the same conclusion.

a. Liquidation Under Chapter 7 or Chapter 11

If neither Alternative under the Plan is confirmed, the Debtor may be forced to liquidate under Chapter 7 of the Bankruptcy Code pursuant to which a trustee would be elected or appointed to liquidate the Debtor's assets for distribution to creditors in accordance with the priorities established by the Bankruptcy Code. It is impossible to predict precisely how the proceeds of the liquidation would be distributed to the respective Holders of Claims against or Interests in the Debtor.

As described above, however, the Debtor believes that in a liquidation under Chapter 7, before creditors received any distribution, additional administrative expenses involved in the appointment of a trustee or trustees and attorneys, accountants and other professionals to assist such trustees would cause a substantial diminution in the value of the Debtor's Estates. The assets available for distribution to creditors would be reduced by such additional expenses and by Claims, some of which would be entitled to priority, which would arise by reason of the liquidation and from the rejection of leases and other executory contracts in connection with the cessation of operations and the failure to realize the greater going-concern value of the Debtor's assets.

MANAGEMENT OF THE COMPANY ESTIMATES THAT THE TOTAL LIQUIDATION PROCEEDS AVAILABLE FOR DISTRIBUTION, NET OF CHAPTER 7 EXPENSES, WOULD AGGREGATE APPROXIMATELY \$257 MILLION TO \$561 MILLION. THIS WOULD RESULT IN A DISTRIBUTION TO CLASS 1 OF LESS THAN 100% OF THEIR CURRENT ALLOWED CLAIMS AND NO DISTRIBUTION TO HOLDERS OF CLASS 5. CONSEQUENTLY, THE COMPANY BELIEVES THAT BOTH THE FL/TELMEX PLAN AND THE STAND-ALONE PLAN, EACH OF WHICH PROVIDES FOR THE CONTINUATION OF ITS BUSINESS, WOULD PROVE A SUBSTANTIALLY GREATER ULTIMATE RETURN TO THE HOLDERS OF SUCH CLAIMS THAN WOULD A CHAPTER 7 LIQUIDATION.

The Debtor also could be liquidated pursuant to the provisions of a Chapter 11 plan of reorganization. In a liquidation under Chapter 11, the Debtor's assets could be sold in an orderly fashion over a more extended period of time than in a liquidation under Chapter 7. Thus, a Chapter 11 liquidation might result in larger recoveries than in a Chapter 7 liquidation, but the delay in distributions could result in lower present values received and higher administrative costs. Because a trustee is not required in a Chapter 11 case, expenses for professional fees could be lower than in a Chapter 7 case. However, any distribution to the Holders of Claims under a Chapter 11 liquidation plan probably would be delayed substantially.

Although preferable to a Chapter 7 liquidation, the Debtor believes that any alternative liquidation under Chapter 11 is a much less attractive alternative to creditors than either Alternative under the Plan because of the greater return the Debtor anticipates either Alternative under the Plan provides.

G. After the Restructuring

Upon consummation of an Alternative under the Plan the Company intends to continue as an operating entity and provide telecommunications services to its customers.

H. Support for the Restructuring

Senior Secured Lenders holding \$584,990,000 in aggregate principal amount of the Senior Credit Facility (approximately 58% of Class 1 Claims) support the FL/Telmex Plan and have executed the Bank Plan Support Agreement, dated June 13, 2002, attached hereto as Appendix E, requiring them, subject to certain conditions, to vote in favor of a plan implementing the terms of the Investment Agreement.

The Administrative Agent has delivered the Bank Stand-Alone Support Letter, dated July 16, 2002, attached hereto as Appendix F. On July 18, 2002, a subgroup of the Senior Lenders Committee and the Official Committee of Unsecured Creditors reached an agreement on certain modifications to the Stand-Alone Term Sheet reflected in the Stand-Alone Plan. On July 19, 2002, the Senior Lenders Committee informed the Bankruptcy Court that the Senior Lenders Committee would support both the FL/Telmex Plan and the Stand-Alone Plan.

On July 19, 2002, the Official Committee of Unsecured Creditors informed the Bankruptcy Court that based upon the negotiations between the Senior Lenders Committee and the Official Committee of Unsecured Creditors, the Official Committee of Unsecured Creditors would support both the FL/Telmex Plan and the Stand-Alone Plan.

I. Estimated Fees and Expenses

The Debtor estimates that fees and expenses incurred in connection with the restructuring will be approximately \$59 million, consisting of:

- up to \$14 million in the fees and expenses of the Investors, as required reimbursements pursuant to the terms and conditions of the Investment Agreement (excluding expenses incurred in enforcing any provision of the Investment Agreement or related document); and
- up to \$45 million in fees and expenses related to the Investment and/or the Stand-Alone Term Sheet, including, without limitation, fees and expenses of brokers, agents, accounting firms, investment banks, other financial advisors, commercial banks, other financial institutions, law firms and public relations firms, but excluding (A) expenses with respect to the settlement of litigation related to the Investment and (B) the Company's obligation to pay the expenses of the Senior Secured Lenders or any commercial bank or other financial institution in connection with the Amended and Restated Credit

Facility or the Exit Facility and the issuance of the Post-Termination Securities.

The Debtor anticipates that a substantial portion of the fees referenced above will be paid at the consummation of the Plan.

J. Recommendation of the Restructuring

XO's Board of Directors and, in certain instances, a subcommittee thereof composed of disinterested, non-management directors considered a number of alternatives with respect to restructuring XO's capital structure, held lengthy meetings, discussed the restructuring with its advisors and, through senior management and advisors, engaged in extensive negotiations with representatives of the Investors regarding the FL/Telmex Plan, the Icahn Group regarding the Icahn Proposal, and the Senior Lenders Committee regarding the Stand-Alone Plan. In addition, the Board of Directors, through senior management and advisors, were involved in negotiations with the Senior Lenders Committee and with the Senior Note Committee regarding the terms of the treatment of the Senior Notes under both the FL/Telmex Plan and the Stand-Alone Plan. See "III. Overview of the Plan and Chapter 11 Case – B. Background." After considering the alternatives, and in light of these extensive negotiations, the Board of Directors approved the petition and the Plan

THE DEBTOR BELIEVES THAT THE CONSUMMATION OF EITHER ALTERNATIVE UNDER THE PLAN WILL ENABLE THE DEBTOR TO SUCCESSFULLY REORGANIZE AND ACCOMPLISH THE OBJECTIVES OF CHAPTER 11 AND THAT ACCEPTANCE OF BOTH THE FL/TELMEX PLAN AND THE STAND-ALONE PLAN IS IN THE BEST INTERESTS OF THE DEBTOR AND THE HOLDERS OF CLASSES 1, 5 AND 6 CLAIMS.

THE DEBTOR, THE SENIOR LENDERS COMMITTEE AND THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS ALL STRONGLY RECOMMEND THAT HOLDERS OF CLASSES 1, 5 AND 6 CLAIMS VOTE TO ACCEPT BOTH THE FL/TELMEX PLAN AND THE STAND-ALONE PLAN.